Frequently Asked Questions on the Standards of GRAP

These FAQs focus on amendments to the Standard of GRAP on *Financial Instruments (revised 2019)*

Disclaimer

These Frequently Asked Questions have been prepared by the Secretariat of the Accounting Standards Board in consultation with the technical division of the Auditor-General of South Africa (AGSA) and the Office of the Accountant-General at National Treasury (OAG). These Frequently Asked Questions have not been approved by the Board. Consequently, they are not authoritative and do not form part of the Standards of Generally Recognised Accounting Practice (GRAP).

The questions and responses outlined in this document are based on queries commonly received by the Secretariat, the AGSA and the OAG and have been compiled to assist preparers of the financial statements. The questions and responses provide a summarised analysis of topical issues and are not comprehensive. Any examples provided are illustrative only and do not represent a comprehensive list of scenarios or circumstances that may exist in practice. As a result, the examples are not prescriptive and should not be used by analogy to other circumstances. In all instances, readers are encouraged to refer to the relevant Standard of GRAP, Interpretation of the Standards of GRAP or Directive.

The Standards of GRAP apply only to material items. Consequently, the FAQs have been drafted on the basis that a particular issue is material. When considering the FAQs, entities should apply judgement in determining whether an issue outlined in the FAQs is material to its operations.

The questions and responses focus on issues that are of interest to public entities, constitutional institutions, municipalities, municipal entities, Parliament and the provincial legislatures, trading entities and Public Technical and Vocational Training Colleges collectively called “entities” in this document (unless indicated otherwise).

FAQ	Subject
1	How should interest be treated on credit impaired instruments that are subsequently 'cured' (i.e. paid or no longer impaired)?

1. **How should interest be treated on credit impaired instruments that are subsequently 'cured' (i.e. paid or no longer impaired)?**

This FAQ explains how an entity presents amounts recognised in surplus or deficit when a credit-impaired financial asset is subsequently cured (i.e. paid in full or no longer credit-impaired).

When a financial asset becomes credit-impaired, paragraph 5.13(b) of GRAP 104 (2019) requires an entity to calculate interest revenue by applying the 'effective interest rate to the *amortised cost* of the financial asset', i.e. the amount that includes the includes the loss allowance. This results in a difference between:

(a) the interest that would be calculated by applying the effective interest rate to the *gross carrying amount* of the credit-impaired financial asset (i.e. excluding the loss allowance); and

(b) the interest revenue recognised for that asset.

If the financial asset is subsequently no longer credit impaired or the interest revenue is received, it was questioned whether this difference should be recognised as interest revenue or, instead, is required to present it as a reversal of impairment losses.

GRAP 104 defines the following:

- A credit loss as 'the difference between all contractual cash flows that are due to an entity in accordance with the contract and all the cash flows that the entity expects to receive (i.e. all cash shortfalls), discounted at the original effective interest rate…'.
- The gross carrying amount as 'the amortised cost of a financial asset, before adjusting for any loss allowance.'

The gross carrying amount, amortised cost and loss allowance are discounted amounts, and changes in these amounts during a reporting period include the effect of the unwinding of the discount. Paragraph 5.23 of GRAP 104 (2019) requires an entity to 'recognise in surplus or deficit, as an impairment gain or loss, the amount of expected credit losses (or reversal) that is required to adjust the loss allowance at the reporting date to the amount that is required to be recognised in accordance with this Standard.' In applying paragraph 5.23 of GRAP 104 (2019), an entity recognises in surplus or deficit as a reversal of expected credit losses the adjustment required to bring the loss allowance to the amount that is required to be recognised in accordance with GRAP 104 (2019) (zero if the asset is paid in full). The amount of this adjustment includes the effect of the unwinding of the discount on the loss allowance during the period that the financial asset was credit-impaired, which means the reversal of impairment losses may exceed the impairment losses recognised in surplus or deficit over the life of the asset. Paragraph 5.13 also specifies how an entity calculates interest revenue using the effective interest method, i.e. an entity calculates interest revenue on a credit impaired financial asset by applying the effective interest rate to the *amortised cost* of the financial asset, and thus interest revenue on such a financial asset does not include the difference outlined above. Accordingly, an entity is required to present the difference described above as a reversal of impairment losses in the surplus or deficit following the curing of a credit-impaired financial asset.

Extracted from IASB Interpretations Committee (IFRIC) agenda decision March 2019 on 'Curing of a credit impaired financial asset'.